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No. 09-28

Supreme Court, U.S.
FILED
OCT 12 2009
OFFICE OF THE CLERK

In The

Supreme Court of the United States

JACK EASTERDAY,

Petitioner,

vs.

UNITED STATES,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

REPLY BRIEF

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REPLY IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

1. The government does not and cannot dispute that several Courts of Appeals, including the Ninth Circuit, have held that, in at least some instances, a showing of financial hardship may constitute a defense to the civil penalties provided in 26 U.S.C. §§6651 and 6656. *See Diamond Plating Co. v. United States*, 390 F.3d 1035, 1038 (7th Cir. 2004); *East Wind Corp. Inc. v. United States*, 196 F.3d 499, 507-08 (3d Cir. 1999); *Fran Corp. v. United States*, 164 F.3d 814, 819 (2d Cir. 1999); *Van Camp & Bennion v. United States*, 251 F.3d 862 (9th Cir. 2001). Nor does the government dispute that those holdings are in direct conflict with *United States v. Brewery*, 33 F.3d 589, 592 (6th Cir. 1994), which held that financial distress can never constitute reasonable cause for failure to pay payroll taxes.

Instead, the government argues that the split in authority is not implicated by this case because this is a criminal case. If there were material differences between the civil and criminal statutes, this contention might have merit. But the language of the statutes suggests that they should be read in the same way. The civil statute provides that penalties may be imposed for failure to pay payroll taxes unless the failure is "due to reasonable cause and not due to willful neglect." 26 U.S.C. §6651(a). The civil statute implicitly defines reasonable cause as the opposite of willfulness. The criminal statute under which Petitioner was convicted allows criminal penalties to be

imposed for failure to pay payroll taxes where an employer "willfully fails" to pay over payroll taxes. 26 U.S.C. §7202. Section 7202, by requiring willfulness, implicitly creates the same "reasonable cause" exception to liability that is found in section 6651. Because the language should be read to create the same exception in the civil and criminal statutes, the split in circuit authority is applicable to both civil and criminal cases.

At minimum, it is ambiguous whether the "willfulness" requirement of section 7202 incorporates a "reasonable cause" exception. Therefore, the rule of lenity requires that the statute be interpreted to incorporate such an exception. See Steve R. Johnson, *Easterday and the "Inability to Pay" Defense for Tax Crimes*, 124 Tax Notes 787, 795 (Aug. 24, 2009).

Finally, the government offers no practical reason for interpreting the two statutes to allow a "reasonable cause" exception to civil penalties while denying such a defense to criminal defendants. This interpretation of the two statutes creates perverse incentives for federal tax examiners. An IRS auditor who determines that an employer is not paying his payroll taxes because of financial hardship will have two options. Either the auditor can assert civil penalties, in which case the delinquent taxpayer will likely be able to mount a strong defense, or he can refer the case to the Department of Justice for prosecution, where the taxpayer will have no such defense. It makes little sense to interpret any statutory ambiguity to encourage IRS employees to more likely seek

criminal charges in cases where employers have a colorable reasonable cause defense.

2. Mr. Easterday's argument is that the criminal tax statute, like the civil tax statute, should recognize an ability to pay defense. The government responds that in this case, Mr. Easterday did not proffer any evidence that would have made out a successful defense, even under the civil statute. (Opp. at 8.) That is simply false.

Prior to trial, Mr. Easterday informed the district court that he would present an inability to pay defense. He sought to show that he was unable to pay his taxes despite exercising ordinary and reasonable business care, and that paying his taxes would have forced him to shut down his nursing homes. The government argued, however, as a matter of law, that inability to pay is not a defense to prosecutions under §7202. The district court agreed with the government. As a result, it categorically excluded all defense evidence and argument regarding inability to pay and ordinary business care.[1]

This is not a case where the trial court accepted the legal validity of a defense but excluded proffered evidence on the grounds of insufficiency. This is also not a case where evidence aimed at showing a legal

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[1] The district court admitted some defense evidence regarding the operation of petitioner's business as relevant to the willfulness element of §7202. But the evidence was admitted only for that limited purpose. *See* Fed. R. Evid. 105.

defense was admitted at trial but rejected by the jury.[2] Instead, this is a case where the trial court denied the legal validity of the defense itself. The trial court thus (1) rejected any and all evidence offered to prove that defense as immaterial, (2) instructed trial counsel not to argue that defense to the jury, and (3) refused to instruct the jury on the defense. Before the trial began, the entire matter was excluded as legally irrelevant.

In sum, given that the government moved successfully to exclude all such evidence as a matter of law prior to trial, it cannot now argue that Mr. Easterday failed to proffer sufficient evidence to establish the defense.

3. The government argues that certiorari is not warranted because the circuits are now in accord that inability is not a defense to §7202 prosecutions. It admits that there was a circuit split, but in light of the decision below, the split disappeared: "the decision below eliminated the preexisting conflict between the Ninth Circuit and the other circuits." That statement contains a stunning concession.

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[2] If petitioner is successful here and is ultimately re-tried, of course the government will be able to dispute the factual validity of his defense. The government will be permitted to present evidence showing, as a matter of fact, that Mr. Easterday had the ability to pay and did not exercise reasonable business prudence.

In the proceedings below, the government adamantly maintained that there was no circuit split because the Ninth Circuit case regarding inability to pay had been long ago overruled by *United States v. Pomponio*, 429 U.S. 10 (1976) (per curiam). That argument was rejected as a convenient fig leaf by dissenting Judge N.R. Smith, but it was accepted by the two-judge majority of the Ninth Circuit panel. The government now admits that its argument below was, in fact, a fig leaf. It admits that *United States v. Poll*, 521 F.2d 329 (9th Cir. 1975), was good law in the Ninth Circuit (and thus that there was a circuit split) until it was overruled in *United States v. Easterday*. It essentially admits that it induced the panel below to violate the law by overruling a prior case without convening an en banc panel.

Admittedly, the Ninth Circuit certainly had the ability to overrule *Poll* by convening an en banc panel – and perhaps it would have done so had the three-judge panel ruled differently. The decision of the panel may have spared the court the trouble of following its own cumbersome and costly en banc procedures. Whether a circuit court follows its own law regarding en banc proceedings is not a matter that justifies certiorari. But the government's sudden (and perhaps unintentional) candor here demonstrates the lengths to which it will go in order to obtain and maintain a criminal conviction.

4. In his petition, Mr. Easterday argued that certiorari is justified in order to clarify whether necessity is a defense – both to federal crimes generally,

and more specifically to the specific crime at issue here, 26 U.S.C. §7202. The government argues that since the circuit courts are now in agreement on the specific question, there is no need to resolve the general question either. (Opp. at 8-9.) That conclusion, however, simply does not follow – the general question is, as this Court has previously recognized, a difficult and important question.

No one disputes that Congress has the power to specify whether necessity is or is not a defense to a particular crime. Put differently, petitioner is not arguing that a necessity defense is constitutionally required for every federal crime. The question, rather, is how courts should treat a statute where Congress fails to take a clear position – where it fails to specify whether necessity is or is not a defense. The question, in other words, is what the default rule is. *Cf.* Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 Yale L.J. 87 (1989).

This Court has never specified a default rule for federal criminal law. As a result, lower courts are free to engage in a statute-by-statute analysis. Lower courts fill in the gaps not by reference to a default, but rather by reference to their own sense of what the best policy choice is in a particular case. In short, the absence of a clear default rule is a license for judicial legislation in the area of the criminal law. The mere fact that all of the circuit courts have now reached the same policy result with respect to §7202 does

nothing to lessen the importance of the general question.

This Court should grant certiorari to set a default rule – one way or the other – in order to limit the largely unfettered discretion that lower courts currently have to accept or reject necessity defenses. Setting a default rule – one way or the other – would replace ad hoc policy analysis with something more principled. Even if this Court were to set a "no necessity defense" default rule, and thus affirm the result reached by the court below, it would greatly improve the state of the law surrounding the necessity defense. This case provides a perfectly appropriate vehicle to address this important question.

CONCLUSION

For the foregoing reasons stated above and in the petition, certiorari should be granted on the important questions raised by petitioner.

Dated: October 12, 2009

Respectfully submitted,

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